

MULTIMEDIA



UNIVERSITY

STUDENT IDENTIFICATION NO

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MULTIMEDIA UNIVERSITY

FINAL EXAMINATION

TRIMESTER 2, 2015/2016

BAC4674 – INTEGRATED CASE STUDY

(All Sections / Groups)

12 MARCH 2016
2.30 PM – 5.30 PM
(3 Hours)

INSTRUCTIONS TO STUDENT

1. This Question paper consists of 11 pages with 6 questions only.
2. Attempt ALL questions. The distribution of the marks for each question is given.
3. Please write all your answers in the Answer Booklet provided.

Adapted from Mohamed Ghows, A.H. et al. (2011) Proton – From Saga to Exora. *Asian Journal of Case Research*, 4 (S), 61-77.

Overview of the Automotive Market

Malaysia: The biggest automobile customer market in South-East Asia

The history of the Malaysian automotive industry dates back to the early 1960s, when the Malaysian government developed a policy to promote an integrated automotive industry to strengthen its industrial base and reduce its dependency on the agricultural sector. The main objective of the promotion of the automotive industry constituted the limitation of imports, the reduction of expenses in foreign exchange, the creation of employment and the development of the industrial sector. Even nowadays, the automotive industry is designated to boost the country's industrialization process and to enable it to reach the status of a developed nation by 2020. The Malaysian national automotive industry is not only one of the major industrial sectors, but also represents a matter of national pride. In terms of fact and figures, the sector ranks amongst the top 20 in the world and disposes of the largest passenger car market in the ASEAN region.

In the 1960s and 1970s, the industry was fragmented and consisted of inefficient assembly plants. The industry's progress to a well-developed manufacturing sector with regards to motor vehicles as well as components can be traced back to numerous government incentives that were initiated in the mid-1980s and remain until today. As a result of this policy two national car projects – Proton, which commenced operation in 1985, and Perodua, which was founded in 1994 – dominate the automotive industry commanding 26% and 30 % respectively of the local market. In the non-national car segment, Nissan held 6.5% of the market, while Toyota held 18% and Honda 6%.

The entry of Proton into the local automobile market resulted in massive structural changes in the industry. The industry shifted from assembly activity to manufacture of vehicles and automotive parts. The sales and the market share of Japanese cars, which had dominated the market prior to the launch of Proton, were reduced as Malaysians bought their national car. The success stories of Proton and Perodua were positively influenced by high tariffs imposed by the government. Many analysts viewed the protectionist policies implemented by the Malaysian government as the most intervening among ASEAN countries. As a consequence, national cars' market share amounted more than 59% of the total sales in 2009 and the market share of the two big Malaysian car manufacturers Proton and Perodua still accounted to 59% in February 2011.

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In 2006 the government introduced the National Automotive Policy (NAP) that envisions the progressive liberalization of the car market through strategic tie-ups and alliances in order to eliminate competition.

Today, with the opening of the market due to the ASEAN Free Trade Agreement (AFTA) the national cars domestic market share has dropped to less than 60%. In ASEAN Malaysia is the third biggest car market with 3 car manufacturers, 8 car assemblers, 9 motor assemblers and more than 800 component manufacturers and employs more than 300,000 people. National car dominance is expected to decline further with more liberalization in the near future.

In the Government's 2012 budget, several incentives for further development of the domestic automotive industry were announced to be continued. Following global trend of environmental friendly vehicles and fuel efficiency, 100 percent exemption for import and excise duties was proclaimed to be continued until 31 December 2013.

Car imports and protectionist policies

To protect the local automotive industry, a number of import restrictions were imposed on foreign vehicles.

With more than half a million sales per year, Malaysia is the biggest market for automobiles in South-East Asia. For a long time Malaysia's government has protected its auto industry from foreign competition by introducing an Asian material content policy, which included imposing high tariffs as well as non-tariff barriers. "National autos", those manufactured by Malaysian producers such as Proton and Perodua, benefit from preferential treatment compared to "nonnational" autos.

The latter category includes even those automobiles that are manufactured in Malaysia by foreign-owned companies. High excise duties, import duties of about 30% (non-ASEAN) and so-called Approved Permits (APs) also belong to these restrictions. The Ministry of International Trade and Industry (MITI) issues the latter only to qualified local personnel and companies, which is the main reason for foreign companies to cooperate with local partners. However, measures have already been undertaken to reduce trade barriers, as the government is forced to abolish this policy within the near future due to its obligations in the World Trade Organization (WTO) and in the ASEAN Free Trade Agreement (AFTA). So far duties are defined separately for Motor Cars, Four Wheel Drive Vehicles, others (like MPVs and Vans and Commercial Vehicles) and whether the cars are from ASEAN or non-ASEAN countries. The duties can vary and depend on the engine capacity as well as if the car was imported in CBU (Completely Built Up), CKD (Completely Knocked Down) or MSP (Multi-Sourcing Parts) form. Irrespective of the form of import, local taxes (Excise Duties and Sales Taxes) are imposed even on cars from ASEAN countries.

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Production

Malaysia has now become one of the region's largest auto markets with vibrant production activities. Currently, there are four National Automotive Projects in Malaysia:

- Perusahaan Otomobil Nasional Bhd (Proton)
- Perusahaan Otomobil Kedua Nasional (Perodua)
- Industri Otomotif Komersial (Inokom)
- Malaysian Truck and Bus (MTB)

Furthermore nine assemblers settled down in Malaysia, among them the Naza Automotive Manufacturing Sdn. Bhd (NAZA) and Honda Sdn. Bhd. Renowned international brands, such as BMW, Landrover, Mercedes Benz, Peugeot, Renault, Scania from Europe and Nissan, Toyota, Mitsubishi and Mazda from Japan are contracting and operating through the local Manufacturing and Assembly Plants in Malaysia in order to fulfill the local content requirements.

In 2011 the total production of motor vehicles amounted to 533,515 units, comprising 488,261 units of passenger vehicles and 45,254 of commercial vehicles. At present the automotive industry employs 47,574 workers, with 25,111 workers employed in the motor vehicle assembly industry and 22,463 workers employed in the motor vehicles parts and accessories industry.

Table 1: Motor Vehicle Production

Year	Passenger Vehicles		Commercial Vehicles		4x4 Vehicles		Total Vehicles	
	Units	% Change	Units	% Change	Units	% Change	Units	% Change
2007	403,245	6.7	38,433	-60.2			441,678	-12.2
2008	484,512	20.2	46,298	20.5			530,810	20.2
2009	447,002	-7.7	42,267	-8.7			489,269	-7.8
2010	522,568	16.9	45,147	6.8			567,715	16.0
2011	488,261	-6.6	45,254	2.4			533,515	-6.0

Source: Malaysian Automotive Association

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Market shares

Considering the market shares in December 2011 both national carmakers continued to dominate the market with a total share of 56%. Foreign company Toyota was outperforming against its two other major non-national peers (Nissan, Honda) with 86,951 units sold despite a decrease of its sales volume. Meanwhile Honda increased its sales volume to 32,480 units while Nissan's market share maintained at 5% with a smaller increase rate of the sales volume. All companies are using a significant proportion of components in their local assemblies from other ASEAN countries, such as Thailand and Indonesia.

Table 2: Market Position by Make/Franchise Holder in Malaysia (January – December 2011)

Ranking	Car Maker	Total	Share
1	Perodua	179,989	30.0%
2	Proton	158,657	26.4%
3	Toyota	86,951	14.5%
4	Honda	32,480	5.4%
5	Nissan	32,276	5.4%
6-40	Others	109,770	18.3%

Source: Malaysian Automotive Association

Background of Proton

Incorporated on 7 May 1983, Proton pioneered Malaysia's venture into the heavy industries and its main objectives are:

- To spearhead the automotive industrialisation process and manufacturing industries;
- To acquire/upgrade technology and industrial skills within the automotive manufacturing industry; and
- To strengthen the international competitiveness of Malaysia's industrial capability

With substantial capital investment over the last quarter of a century and the corporate philosophy that success can be achieved by having 'the right car for the right market, at the right price and at the right time', Proton commands a substantial share of the domestic market for passenger cars and through the years, has expanded its international footprint such as Thailand, Indonesia, Egypt, Syria and Australia.

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Proton's business activities span throughout the whole automotive value chain encompassing vehicle engineering, research and development, manufacturing, distribution, sales, after-sales services as well as financing.

The foundation of the Group's growth is due to the understanding of the economic development stimulus, diverse customer needs and the ability to translate them into products that customers want, through research and development.

The current portfolio of Proton models includes the Saga, which was named Best Model of the Year for two consecutive years 2009 and 2010; the Persona, winner of the 2008 Asean Automotive Award for Best Model of the Year; the stylish Gen.2; the fun-to drive Savvy; the desirably sporty Satria Neo; Malaysia's first home-grown multipurpose vehicle (MPV), the Exora; as well as the Inspira.

Also in the Group's portfolio, is the world-renowned Lotus sportscar brand, with models such as Elise, Exige, Europa and the Evora, the latest supercar that remains true to Lotus' heritage and core philosophies of being Visually Stunning, Exhilarating, Agile and Responsive, to suit a range of customer demands and preferences.

With the Group's spirit of achievement, the industry has recognised the Company's efforts and bestowed these awards on Proton in 2010/2011:

- Frost & Sullivan Malaysia Excellence Awards 2010 – Best Passenger Car Model of the Year for Proton Saga
- Frost & Sullivan Malaysia Excellence Awards 2010 – Best Automotive Debut Model of the Year for Exora
- CIMB Autoworld Car of the Year Awards 2010 – Best MPV - Overall Value-for-Money for Exora
- Labour Day Achievement Award for the category Competitive Employer Award (Big Corporations) in conjunction with 2010 Workers' Day Celebrations
- MITI Industry Excellence Award for the category Quality Management Excellence Award
- Reader's Digest Trusted Brand 2011 Gold Award for Car Category
- Frost & Sullivan Malaysia Excellence Awards 2011 – Value-for-Money Car of the Year (1.3L and above) for the Proton Persona
- Indonesian Otomotif Awards – “Best Budget MPV in Indonesia” for the Exora
- Asian Auto – Auto Industry Awards 2011 – “Best People's Car” for the Saga FL and “Best Value-for-Money Family Car” for the Inspira

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As a global automotive challenger, the Group conducts research in its centres throughout the world, on new technologies to create cars that are unique in both design and driving performance. Through Lotus, the Group provides comprehensive and versatile consultancy services to many of the world's OEMs and Tier 1 suppliers. Today, Group Lotus is organized into two business divisions. Lotus Cars focuses on sales of world-class, prestigious, high-performance sports cars, whilst Lotus Engineering provides engineering solutions for automotive manufacturers and suppliers.

To boost the quality of its products, Proton performs a continuous Company-wide quality improvement programme and quality-conscious work culture that assures:

- Quality in everything (products and individuals);
- Quality in the way things are done (doing it right the first time);
- Quality in spending, including reducing materials costs;
- High-quality products (end products must be of the right technology and designed to meet market expectations); and
- Quality services to customers, including after-sales support.

With staff strength close to 12,000 employees worldwide, Proton ensures that each individual is aligned to their core values, thereby ensuring strong customer orientation in order to produce competitive products that drive business forward.

Export market

The Proton export business was expected to grow exponentially throughout the fiscal years given a series of positive outcome recorded in the same period of the previous year. However, despite the normal anticipation based on the growth of demand for Proton cars, some unexpected challenges arose and resulted in revisions on implementation approaches in some markets, such as China, Australia and the Middle East region.

Disposal of MV Augusta

Proton had disposed of MV Agusta in December 2005 in an exercise to divest its non-core assets. Proton had originally acquire MV Agusta for €70 million in July 2004, on top of taking on its debts. It finally sold it to Gevi SpA for €1 (RM4.48), together with its debts and working capital requirements of €139.44 million. In July 2008, Harley-Davidson signed an agreement to purchase 100% of MV Agusta for €70 million (RM355 million).

Joint venture with Goldstar

Proton is being sued for alleged breach of contract by its former Chinese joint-venture partner, Goldstar Heavy Industrial Co Ltd. Goldstar is seeking about one billion yuan (RM520mil) in compensation for the failed venture.

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Under a joint-venture proposal signed in 2002, a plant was to be set up in Dongguan to manufacture cars. Proton claimed that Goldstar failed to obtain a licence for the joint venture within three years, frustrating its initiative to start manufacturing cars in China. The joint venture will help Proton cut costs and become more competitive in the market and create more jobs and economic benefits for Malaysia.

Business turnaround

Looking at the dramatic turnaround Proton has undergone in the past six years spearheaded by Khazanah Nasional Berhad, the investment arm of the Government of Malaysia, and the single largest substantial shareholder in Proton, was reported to have said that Proton needed a strategic partner and strategic alliance to enable a sustainable turnaround. The global economic crisis had accelerated the pace of consolidation across many industries and automotive manufacturers were no exception. Many planned strategies had to be put on hold. The turnaround of Proton is expected to take longer than expected as the national carmaker continues to record moderate profit and see its market share shrink.

Proton Strategies Facing the Challenges

Internal growth

After the discontinuation of the partnership with Mitsubishi Motor Corporation, Japan in 2004, public perception towards Proton cars suffered due to reported poor product quality control and non-descript designs. In addition, its declining financial performance over the last several years had been dismal, despite its acquisitions of the Lotus Group (UK) in 1996 and MV Augusta (Italy) in 2004 to further its quest for better technology.

Foreign partnerships

Strategic discussion with several foreign automobile manufacturers did take place. In April 2009, it was reported that Proton had engaged in early discussions with Renault SA and GM on the possibility of technical alliances. In September 2009, Proton was said to be talking with VW on a strategic partnership that would see Volkswagen cars assembled at Proton's Tanjung Malim plant in Malaysia. It was understood that Proton could leverage on VW's worldwide marketing network as a platform to market Proton cars internationally.

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Management buy-out

The future of Malaysia's first national car company, Proton has come into focus once again after the company's chairman Datuk Mohd Nadzmi Mohd Salleh confirmed he is considering leading a management buy-out of the company if the Malaysian government was prepared to sell a controlling stake. He pointed out that Proton has the potential to become a significant regional player if it was given the entrepreneurial spirit it lacks, together with some additional innovation and creativity. Proton is fairly well managed and financially strong, and that the task of turning it around would not be too difficult. Other domestic companies interested in taking over Proton Holdings include DRB-HICOM Bhd and Yasmin Holdings Sdn Bhd.

Summary of Financial Highlights

The following are Proton's Statement of Comprehensive Income and Statement of Financial Position for the period between 2007 and 2011.

Statements of Comprehensive Income for the financial year ended 31 March

RM mil	2011	2010	2009	2008	2007
Revenue	8,969.9	8,226.9	6,486.6	5,621.6	4,687.3
Profit/(Loss) before taxation	214.4	260.9	(319.2)	144.3	(618.1)
Profit/(Loss) after taxation	155.6	218.9	(301.8)	184.6	(589.5)
Retained earnings attributable to shareholders	4,526.4	4,372.8	4,174.5	4,476.2	4,319.2
Dividend paid	(82.4)	-	(20.6)	-	(27.5)
Retained earnings carried forward	4,444.0	4,372.8	4,153.9	4,476.2	4,291.7
Share Information per Share					
Basic earnings/(loss) (sen)	28.3	39.9	(54.9)	33.6	(107.3)
Dividend paid (sen)	20.0	-	5.0	-	5.0
Net assets (RM)	9.8	9.7	9.3	9.9	9.5
Issued share capital ('000)	549,213	549,213	549,213	549,213	549,213

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Statements of Financial Position

as at 31 March

RM mil	2011	2010	2009	2008	2007
Non-Current Assets					
Property, plant and equipment	2,529.9	2,624.4	2,827.1	3,174.5	3,179.4
Goodwill	29.0	29.0	29.0	29.0	29.0
Intangible assets	877.4	564.0	431.7	275.2	169.1
Associated companies	151.3	152.6	158.4	165.4	169.8
Jointly controlled entities	215.5	202.6	195.6	192.7	223.6
Investments	-	-	10.4	10.4	10.4
Deferred tax assets	16.7	15.0	5.7	-	-
Total Non-Current Assets	3,819.8	3,587.6	3,657.9	3,847.2	3,781.3
Current Assets					
Inventories	1,207.1	1,227.2	1,395.1	1,100.3	1,273.6
Receivables	1,329.5	991.6	1,080.3	1,099.0	1,192.0
Available-for-sale financial assets	4.5	-	-	-	-
Current investments	-	9.7	15.3	20.8	73.4
Deposits, bank and cash balances	1,293.0	1,652.1	913.9	1,226.0	626.5
Total Current Assets	3,834.1	3,880.6	3,404.6	3,446.1	3,165.5
Non-current assets held for sale	-	36.9	36.4	-	-
Total Assets	7,653.9	7,505.1	7,098.9	7,293.3	6,946.8

RM mil	2011	2010	2009	2008	2007
Equity					
Share capital	549.2	549.2	549.2	549.2	549.2
Other reserves	413.5	411.0	398.5	395.8	389.7
Retained profits	4,444.0	4,372.8	4,153.9	4,476.2	4,291.7
Equity attributable to equity holders of the company	5,406.7	5,333.0	5,101.6	5,421.2	5,230.6
Minority interest	-	-	-	-	-
Total Equity	5,406.7	5,333.0	5,101.6	5,421.2	5,230.6
Non-Current Liabilities					
Long term liabilities	28.2	59.1	49.3	99.7	105.4
Long term borrowings	9.8	29.6	52.2	130.8	76.2
Deferred tax liabilities	8.2	10.7	12.2	2.4	0.8
Total Non-Current Liabilities	46.2	99.4	113.7	232.9	182.4
Current liabilities					
Payables	1,826.6	1,918.4	1,571.3	1,524.0	1,367.2
Short term borrowings	361.5	142.2	306.0	113.6	164.4

Taxation	12.9	12.1	6.3	1.6	2.2
Total Current Liabilities	2,201.0	2,072.7	1,883.6	1,639.2	1,533.8
Total Liabilities	2,247.2	2,172.1	1,997.3	1,872.1	1,716.2
Total Equity and Liabilities	7,653.9	7,505.1	7,098.9	7,293.3	6,946.8

National Automotive Policy (NAP)

Given the significant challenges facing the automotive industry, in particular globalization, economic liberalization and increasing competition, the Malaysian government felt that there is a need to review the strategic direction and policy framework for the domestic automotive sector. This change towards a less regulated policy is crucial to maintain the competitiveness of the domestic automotive sector in the country and internationally and to make it thus viable in the long term. Having this in mind, the government launched the National Automotive Policy (NAP) in March 2006, which primarily aims at progressive market liberalization. In September 2009, the NAP was revised to encourage new investments, ensure a long term sustainability of the domestic automotive industry, ensure safety and quality of products and services and protection of the environment. Some highlights on the revised NAP:

- Manufacturing licence - Local assembly of luxury passenger cars above 1,800 cc or priced above RM150,000 is fully liberalized. This means foreign firms are allowed to obtain manufacturing licence and can hold 100% equity in the companies. However, current policy on the freeze of manufacturing licence for reconditioning and reassembling activities is maintained.
- Amendments to the AP System (Approval Permit) - The issuance of APs will be stopped by end 2015.
- Incentives - Incentives such as Pioneer Status/Investment Tax Allowance for the manufacture of critical components for cars such as brake system and transmission.
- Safety standards - There would be a gradual introduction of Vehicle End of Life Policy. Vehicles above 15 years will have to undergo mandatory inspection during road tax renewal.
- Euro 4m specification - Implementing Euro 4m specification for petrol and diesel in 2011.
- Tax/Duty - The Import Duty structure is maintained at 0% for CKD and 5% for CBU for AFTA. As for Excise Duty, there are no changes.
- Imports - From June 2011, it would be prohibited to import used parts/components.
- Establishment of a strategic partnership for Proton - The quest is on for Proton to have a strategic partnership with a globally established manufacturer.

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Required:

- (a) Identify the issues that require immediate attention by the Proton's management.
(10 marks)
- (b) Analyze the financial statements of Proton for the years 2007 to 2011. What can you say about the company's efficiency and profitability? Use relevant ratios to support your answer.
(20 marks)
- (c) The best way for Proton to move forward is to collaborate with a foreign strategic partner such as Renault SA, General Motors and Volkswagen. Explain.
(5 marks)
- (d) Technology and innovation are the driving forces behind Proton's Engineering Services Division as the group continues to progress with pride and passion in product development, styling and technology development, collaborations, people development and process improvements. How can Proton continue to successfully inculcate a culture of innovation among its people?
(5 marks)
- (e) In mid-September 2009 and early October 2009, it had been reported that Tan Sri Syed Mokhtar Al-Bukhary and Datuk Kisai Rahmat were interested in buying Khazanah's 42.74% stake in Proton via DRB-HICOM. Identify the factors or information that they would consider prior to the takeover process.
(10 marks)
- (f) "The 2009 National Automotive Policy, on the whole, is said to benefit Proton". Discuss the statement.
(10 marks)

(Total: 60 marks)

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